

COMMONWEALTH OF KENTUCKY  
BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of:

|   |            |
|---|------------|
| ELECTRONIC APPLICATION OF LYON COUNTY ) | CASE NO.   |
| WATER DISTRICT FOR A RATE ADJUSTMENT )  | 2021-00391 |
| PURSUANT TO 807 KAR 5:076 )             |            |

NOTICE OF FILING OF COMMISSION STAFF'S REPORT

Notice is hereby given that, in accordance with the Commission's Order of January 13, 2022, the attached report containing the recommendations of Commission Staff regarding the Applicant's proposed rate adjustment has been filed in the record of the above-styled proceeding. Pursuant to the Commission's December 14, 2021 Order, Lyon County Water District (Lyon District) is required to file written comments regarding the recommendations of Commission Staff no later than 14 days from the date of this report. The Commission directs Lyon District to the Commission's July 22, 2021 Order in Case No. 2020-00085<sup>1</sup> regarding filings with the Commission.



Linda C. Bridwell, PE  
Executive Director  
Public Service Commission  
P.O. Box 615  
Frankfort, KY 40602

DATED APR 06 2022

cc: Parties of Record

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<sup>1</sup> Case No. 2020-00085, *Electronic Emergency Docket Related to the Novel Coronavirus COVID-19* (Ky. PSC July 22, 2021), Order (in which the Commission ordered that for case filings made on and after March 16, 2020, filers are NOT required to file the original physical copies of the filings required by 807 KAR 5:001, Section 8).

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| PURSUANT TO 807 KAR 5:076 )             |            |

COMMISSION STAFF'S REPORT ON  
LYON COUNTY WATER DISTRICT

Lyon County Water District (Lyon District) is a water utility organized pursuant to KRS Chapter 74 that owns and operates a water distribution system through which it provides retail water service to approximately 2,666 residential customers and 39 commercial customers in Lyon County, Kentucky.<sup>1</sup> In the final Order for Case No. 2019-00444,<sup>2</sup> Lyon District was ordered to file an application by June 15, 2021, for a general adjustment in rates pursuant to 807 KAR 5:001 Section 16, or an alternative rate filing pursuant to 807 KAR 5:076. However, Lyon District did not file an application by June 15, 2021, and on October 1, 2021, Case No. 2021-00343<sup>3</sup> was initiated to investigate, among other things, allegations that Lyon District's board of commissioners violated the Commission's June 15, 2020 Order in Case No. 2019-00444. On November 15, 2021, Lyon District tendered its application to the Commission requesting to adjust its water

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<sup>1</sup> *Annual Report of Lyon District to the Public Service Commission for the Calendar Year Ended December 31, 2020* (2020 Annual Report) at 12 and 49.

<sup>2</sup> Case No. 2019-00444, *Electronic Proposed Adjustment of the Wholesale Water Service Rates of Princeton Water and Wastewater* (Ky. PSC June 15, 2020).

<sup>3</sup> Case No. 2021-00343, *Electronic Alleged Failure of Lyon County Water District and Its Individual Commissioners Don Robertson and Charles Murphy, and Superintendent, William Asher, to Comply with KRS 278.230, 807 KAR 5:006, SEC. 4(2), and KRS 278.990* (Ky. PSC Oct. 1, 2021).

rates pursuant to 807 KAR 5:076. On December 13, 2021, in response to the filing of the application, the Commission held Case No. 2021-00343 in abeyance. The Order also incorporated the case record of Case No. 2021-00343 into this proceeding.<sup>4</sup>

To ensure the orderly review of the application, the Commission established a procedural schedule by Order dated December 14, 2021. Commission Staff's First Request for Information (Staff's First Request) was filed and the procedural schedule was amended on January 13, 2022. Commission Staff's Second Request for Information (Staff's Second Request) was filed on February 23, 2022.

WATER LOSS

Pursuant to 807 KAR 5:066(6)(3), water loss is limited to 15 percent for ratemaking purposes. In its 2020 Annual Report, Lyon District reported a water loss of 19.82 percent.<sup>5</sup> The annual cost to Lyon District for water loss above the allowable 15 percent is \$18,926.<sup>6</sup> The annual cost of total water loss is \$77,777.<sup>7</sup> Failure by Lyon

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<sup>4</sup> *Id.* (Ky. PSC December 13, 2021), Order.

<sup>5</sup> 2020 Annual Report at 57.

<sup>6</sup>

|                                    | Purchased<br>Water |
|------------------------------------|--------------------|
| Pro Forma Purchased Water          | \$ 392,346         |
| Times: Water loss in excess of 15% | 4.82%              |
| <br>                               |                    |
| Total Cost of Excess Water Loss    | \$ 18,926          |

<sup>7</sup>

|                           | Purchased<br>Water |
|---------------------------|--------------------|
| Pro Forma Purchased Water | \$ 392,346         |
| Times: Total Water loss   | 19.82%             |
| <br>                      |                    |
| Total Cost of Water Loss  | \$ 77,777          |

District to make significant progress towards reducing unaccounted-for water loss may cause the Commission to pursue additional action with the utility.

To comply with the requirements of 807 KAR 5:076, Section 9,<sup>8</sup> Lyon District used the calendar year ended December 31, 2020, as the basis for its application. Using the Debt Service Coverage (DSC) method and its pro forma test-year operations, Lyon District determined that a revenue increase of \$198,315, or 14.62 percent over test-year normalized revenues of \$1,554,660, was warranted<sup>9</sup> as shown in the table below. The rates requested by Lyon District would increase the residential monthly bill of a typical residential customer using 4,000 gallons per month by \$6.99 from \$47.76 to \$54.75, or approximately 14.62 percent.<sup>10</sup>

|   | Lyon County<br>Water District |
|---|-------------------------------|
| Pro Forma Operating Expenses                      | \$ 1,205,792                  |
| Plus: Avg. Annual Principal and Interest Payments | 290,723                       |
| Debt Coverage Requirement                         | <u>58,145</u>                 |
| Overall Revenue Requirement                       | 1,554,660                     |
| Less: Interest and Dividend Income                | -                             |
| Nonutility Income                                 | <u>-</u>                      |
| Revenue Required From Water Sales                 | 1,554,660                     |
| Revenue from Sales at Present Rates               | <u>(1,356,345)</u>            |
| Required Revenue Increase                         | <u>198,315</u>                |
| Percentage Increase                               | <u><u>14.62%</u></u>          |

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<sup>8</sup> The reasonableness of the proposed rates shall be determined using a 12-month historical test period, adjusted for known and measurable changes, that coincide with the reporting period of the applicant's annual report for the immediate past year.

<sup>9</sup> Application, Exhibit D.

<sup>10</sup> *Id.*, Exhibit K.

To determine the reasonableness of the rates requested by Lyon District, Commission Staff performed a limited financial review of Lyon District's test-year operations. The scope of Commission Staff's review was limited to determining whether operations reported for the test year were representative of normal operations. Known and measurable<sup>11</sup> changes to test-year operations were identified and adjustments made when their effects were deemed material. Insignificant and immaterial discrepancies were not necessarily pursued or addressed.

Commission Staff's recommendations are summarized in this report. William Foley and Ariel Miller reviewed the calculation of Lyon District's Overall Revenue Requirement. Eddie Beavers and Samuel Leveridge reviewed Lyon District's reported revenues and rate design.

### SUMMARY OF FINDINGS

1. Overall Revenue Requirement and Required Revenue Increase. By applying the Debt Service Coverage (DSC) method, as generally accepted by the Commission, Commission Staff found that Lyon District's required revenue from rates is \$1,445,326 to meet the Overall Revenue Requirement of \$1,447,421 and that an \$88,981 revenue increase, or 6.56 percent, to pro forma present rate revenues is necessary to generate the Overall Revenue Requirement.

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<sup>11</sup> Commission regulation 807 KAR 5:076, Section 9 sets the standard for the determination of the reasonableness of proposed rates and states, in pertinent part, that the test period shall be "adjusted for known and measurable changes." See also Case No. 2001-00211, *The Application of Hardin County Water District No. 1 for (1) Issuance of Certificate of Public Convenience and Necessity; (2) Authorization to Borrow Funds and to Issue its Evidence of Indebtedness Therefore; (3) Authority to Adjust Rates; and (4) Approval to Revise and Adjust Tariff* (Ky. PSC Mar. 1, 2002); Case No. 2002-00105, *Application of Northern Kentucky Water District for (A) an Adjustment of Rates; (B) a Certificate of Public Convenience and Necessity for Improvements to Water Facilities if Necessary; and (C) Issuance of Bonds* (Ky. PSC June 25, 2003); Case No. 2017-00417, *Electronic Proposed Adjustment of the Wholesale Water Service Rates of Lebanon Water Works* (Ky. PSC July 12, 2018).

2. Monthly Water Service Rates. Lyon District proposed to increase all of its monthly retail water service rates by approximately 14.62 percent. Lyon District has not performed a cost of service study (COSS). Lyon District stated that it did not complete a COSS at this time as there has been no material changes in the water system.<sup>12</sup>

In the absence of a cost of service study (COSS), the Commission has previously found that the allocation of a revenue increase evenly across the board to a utility's rate design is appropriate when there has been no evidence entered into the record demonstrating that this method is unreasonable. Finding no such evidence in this case, Commission Staff has followed the method previously accepted by the Commission and has allocated the \$88,981 revenue increase evenly across the board to Lyon District's monthly retail water service rates.

The rates set forth in the Appendix to this report are based upon the revenue requirement, as calculated by Commission Staff, and will produce sufficient revenues from water sales to recover the \$1,445,326 Revenue Required from Rates, an approximate 6.56 percent increase. These rates will increase a typical residential customer's monthly water bill from \$47.76 to \$50.89, an increase of \$3.13, or approximately 6.55 percent.<sup>13</sup>

3. Nonrecurring Charges. Following the Commission's recent decisions,<sup>14</sup> Commission Staff has reviewed Lyon District's Nonrecurring Charges. The Commission

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<sup>12</sup> Staff's First Request (filed Feb. 3, 2022), Item 4.

<sup>13</sup> The typical residential customer uses approximately 4,000 gallons per month.

<sup>14</sup> Case No. 2020-00141, *Electronic Application of Hyden-Leslie County Water District for an Alternative Rate Adjustment* (Ky. PSC Nov. 6, 2020); Case No. 2020-00167, *Electronic Application of Ohio County Water District for an Alternative Rate Adjustment* (Ky. PSC Dec. 3, 2020); Case No. 2020-00196, *Electronic Application of West Daviess County Water District for an Alternative Rate Adjustment* (Ky. PSC

found that, as district personnel are currently paid during normal business hours, estimated labor costs previously included in determining the number of Nonrecurring Charges should be eliminated from the charges. Lyon District provided cost justification information for the Nonrecurring Charges that are listed in its tariff.<sup>15</sup> Commission Staff reviewed the cost justification information provided by Lyon District and have adjusted these charges by removing Field Labor Costs and Office/Clerical Labor Costs. Such adjustments result in the following revised Nonrecurring Charges:

| <u>Nonrecurring Charge</u> | <u>Normal Hours</u> |
|----------------------------|---------------------|
| Meter Read-Out             | \$7.00              |
| Field Collection           | \$7.00              |
| Meter Reconnect            | \$10.00             |
| Meter Re-Read              | \$7.00              |
| Meter Test                 | \$37.00             |
| Returned Check             | \$31.00             |

The adjustments to the Nonrecurring Charges result in a decrease in Other Operating Revenue of \$2,331 as shown below.

| <u>Charge</u>   | <u>Number of Occurrences</u> <sup>16</sup> | <u>Test-Year Revenue</u> | <u>Adjustment</u> | <u>Pro Forma</u> |
|-----------------|--|--------------------------|-------------------|------------------|
| Meter Reconnect | 59   | \$2,950                  | (\$2,360)         | \$590            |
| Returned Check  | 29   | \$870                    | \$29              | \$899            |
| Totals          |  | \$3,820                  | (\$2,331)         | \$1,489          |

### PRO FORMA OPERATING STATEMENT

Lyon District's Pro Forma Operating Statement for the test year ended December 31, 2020, as determined by Commission Staff, appears below.

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Dec. 30, 2020); and Case No. 2020-00195, *Electronic Application of Southeast Daviess County Water District for an Alternative Rate Adjustment* (Ky. PSC Dec. 30, 2020).

<sup>15</sup> Lyon District's Response to Staff's First Request (filed Feb. 10, 2022), Item 7.

<sup>16</sup> Lyon's District's Response to Staff's First Request (filed Feb. 10, 2022), Item 6.

|  | <u>Test Year</u>    | <u>Adjustment</u> | <u>(Ref.)</u> | <u>Pro Forma</u>    |
|--|---------------------|-------------------|---------------|---------------------|
| Operating Revenues                       |                     |                   |               |                     |
| Total Metered Sales                      | \$ 1,239,508        | 116,837           | (A)           | \$ 1,356,345        |
| Other Water Revenues                     |                     |                   |               |                     |
| Misc. Service Revenues                   |                     | 1,489             | (B)           | 1,489               |
| Other Water Revenues                     |                     |                   |               | -                   |
| Total Operating Revenues                 | <u>\$ 1,239,508</u> | <u>118,326</u>    |               | <u>\$ 1,357,834</u> |
| Operating Expenses                       |                     |                   |               |                     |
| Operation and Maintenance Expenses       |                     |                   |               |                     |
| Salaries and Wages - Employees           | 149,462             | 4,540             | (C)           | 154,002             |
| Salaries and Wages - Officers            | 10,800              | 7,200             | (D)           | 18,000              |
| Employee Pensions and Benefits           | 109,357             | (8,414)           | (E)           |                     |
|  |                     | (27,883)          | (F)           |                     |
|  |                     | (12,378)          | (G)           | 60,682              |
| Purchased Water                          | 410,230             | (17,884)          | (H)           |                     |
|  |                     | (18,926)          | (I)           | 373,420             |
| Purchased Power                          |                     |                   |               | -                   |
| Materials and Supplies                   | 73,657              |                   |               | 73,657              |
| Contractual Services                     | 162,172             | (64,734)          | (J)           |                     |
|  |                     | (2,800)           | (K)           | 94,638              |
| Insurance                                | 24,569              |                   |               | 24,569              |
| Miscellaneous Expense                    | 71,680              |                   |               | 71,680              |
| Total Operation and Maintenance Expenses | 1,011,927           | (141,280)         |               | 870,647             |
| Depreciation                             | 317,163             | (103,489)         | (L)           | 213,674             |
| Amortization                             |                     |                   |               |                     |
| Taxes Other Than Income                  | 2,451               | 11,781            | (G)           | 14,232              |
| Utility Operating Expenses               | <u>1,331,541</u>    | <u>(232,988)</u>  |               | <u>1,098,553</u>    |
| Utility Operating Income                 | (92,033)            | 351,314           |               | 259,281             |
| Interest and Dividend Income             | 606                 |                   |               | 606                 |
| Income Available to Service Debt         | <u>(91,427)</u>     | <u>351,314</u>    |               | <u>259,887</u>      |

(A) Billing Analysis. Lyon District proposed to increase its test-year revenues from water sales of \$1,239,508 by \$116,837 to reflect the billing adjustments made during the test year. Commission Staff agrees as Lyon District's adjustment meets the

ratemaking criteria of being known and measurable and accepts the adjustment in Pro Forma operations.

(B) Nonrecurring Charges. Lyon District reported that it collected \$3,820 from nonrecurring charges during the test year.<sup>17</sup> However, Lyon District did not report any income aside from Metered Water Sales.<sup>18</sup> Commission Staff was unable to locate the revenue account Lyon District reported its revenues for nonrecurring charges except for \$610, which was reported to account for 400.02 Reconnection Charges.<sup>19</sup> Commission Staff suspects the remainder was included in the Metered Water Sales. Adjustment (A) mentioned above would remove the nonrecurring revenues from the metered sales, but an additional adjustment to Other Water Revenues is necessary. As explained above, the \$3,820 Miscellaneous Service Revenues needed to be reduced by \$2,331. Therefore, Commission Staff made a net adjustment increasing Miscellaneous Service Revenues by \$1,489.

(C) Salaries and Wages - Employees. In its application, Lyon District reported Salaries and Wages - Employees Expense of \$149,462.<sup>20</sup> Lyon District provided the total number of hours worked during and subsequent to the test year, a current employees list, job responsibilities, and pay rates.<sup>21</sup> Subsequent to the test year, one full-time and four part-time employees left employment, and Lyon District hired two full-

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<sup>17</sup> *Id.*, Item 6.

<sup>18</sup> Application, Exhibit C.

<sup>19</sup> Lyon's District's Response to Staff's First Request (filed Feb. 10, 2022), Item 1a

<sup>20</sup> Application, Exhibit C.

<sup>21</sup> Lyon District's Response to Commission Staff's First Request, (filed Jan 28, 2022), Items 1f and 1g.

time employees.<sup>22</sup> Commission Staff used the information to calculate pro forma Salaries and Wages - Employees expense of \$154,002. Therefore, Commission Staff made an increase to Salaries and Wages - Employees of \$4,540 as shown below.

| Test Year hours with Current Wages |                   |             |                        |                     |                        |                          |                               |                |                       |
|------------------------------------|-------------------|-------------|------------------------|---------------------|------------------------|--------------------------|-------------------------------|----------------|-----------------------|
| Employee ID                        | Employee Position | Total Hours | Test Year Normal Hours | Current Wages Rates | Pro Forma Normal Wages | Test Year Overtime Hours | Pro Forma Overtime Wage Rates | Per task Wages | Total Pro Forma Wages |
| 3                                  | Field Employee    | 2,264       | 2,080                  | \$ 18.03            | \$ 37,502              | 184.25                   | \$ 27.05                      | \$ 4,983       | \$ 42,485             |
| 11                                 | Field Employee    | 2,201       | 2,080                  | 15.25               | 31,720                 | 120.50                   | 22.88                         | 2,756          | 34,476                |
| 12                                 | Superintendent    |             |                        | Salary              | 50,000                 |                          |                               |                | 50,000                |
| 13                                 | Field Employee    | 2,080       | 2,080                  | 13.00               | 27,040                 |                          | 19.50                         |                | 27,040                |
| Total Pro Forma Wages              |                   |             |                        |                     |                        |                          |                               |                | 154,002               |
| Less: Test Year Wages              |                   |             |                        |                     |                        |                          |                               |                | (149,462)             |
| Pro Forma Adjustment               |                   |             |                        |                     |                        |                          |                               |                | <u>\$ 4,540</u>       |

(D) Salaries and Wages - Officers. Lyon District proposed an increase to test year Salaries and Wages Expense- Officers of \$7,200, in order to reflect a normalized test year for an increase in Commissioners’ salaries.<sup>23</sup> Lyon District employs three commissioners who each receive a \$6,000 annual salary.<sup>24</sup> As shown below, annualizing the commissioners’ wages results in a Salaries and Wages - Officer’s Expense of \$18,000. Therefore, Commission Staff agrees with Lyon District’s proposed adjustment of \$7,200 and increased pro forma Salaries and Wages Expense - Officers accordingly.

<sup>22</sup> *Id.* And Lyon District’s Response to Commission Staff’s Second Request, (filed Mar 10, 2022), item 2.

<sup>23</sup> Application, Exhibit C, Adjustment C.

<sup>24</sup> Response to Supplemental Questions Regarding RFI 1, 10\_2021\_Fiscal\_Court\_Minutes.pdf, (Filed Mar 25, 2022).

| <u>Commissioners</u>             | <u>Test Year<br/>Salaries</u> |
|----------------------------------|-------------------------------|
| Charles Murphy                   | \$ 6,000                      |
| Charles Don Robertson            | 6,000                         |
| Chris Sutton                     | 6,000                         |
| <br>Pro Forma Salaries & Wages   | <br>18,000                    |
| Less: Test Year Salaries & Wages | <u>(10,800)</u>               |
| <br>Adjustment                   | <br><u>\$ 7,200</u>           |

(E) Employee Pensions and Benefits- Health Insurance. Lyon District currently pays 100 percent for single health insurance at \$569, \$457, and \$367 per month for each of three full-time employees, respectively. Lyon District also pays all three employees' dental insurance of \$23.92 per employee, per month. The Commission continues to place greater emphasis on evaluating employees' total compensation packages, including both salary and benefits programs, for market and geographic competitiveness to ensure the development of a fair, just and reasonable rate. The Commission has found that, in most cases, 100 percent of employer-funded health care does not meet those criteria.<sup>25</sup>

Consistent with this precedent, Commission Staff reduced Lyon District's single health insurance premiums by 22 percent,<sup>26</sup> and dental insurance premiums by

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<sup>25</sup> Case No. 2020-00167, *Electronic Application of Ohio County Water District for an Alternative Rate Adjustment* (Ky. PSC Dec. 3, 2020). Case No. 2020-00296, *Electronic Application of Allen County Water District for an Alternative Rate Adjustment* (Ky. PSC Feb. 3, 2021).

<sup>26</sup> Bureau of Labor Statistics, Healthcare Benefits, March 2020, Table 3, private industry workers. (<https://www.bls.gov/news.release/pdf/ebs2.pdf>).

60 percent<sup>27</sup> as shown in the calculation below. Accordingly, Commission Staff decreased Employee Pensions and Benefits by \$8,414.

| Type of Premium                 | Employer Contributions | Average Employee Contribution Rate | Monthly Premium Adjustment | Pro Forma Monthly Premium |
|---------------------------------|------------------------|------------------------------------|----------------------------|---------------------------|
| Single Health Insurance         | \$ 1,393               | 22%                                | \$ (306)                   | \$ 1,087                  |
| Dental Insurance                | 72                     | 60%                                | (43)                       | 29                        |
| Total Pro Forma Monthly Premium |                        |                                    |                            | 1,115                     |
| Times: 12 Months                |                        |                                    |                            | <u>12</u>                 |
| Total Annual Pro Forma Premium  |                        |                                    |                            | 13,380                    |
| Less: Test Year                 |                        |                                    |                            | <u>(21,794)</u>           |
| Adjustment                      |                        |                                    |                            | <u>\$ (8,414)</u>         |

(F) Employee Pensions and Benefits - Retirement. Lyon District provides pension and post-retirement health care benefits to its employees by participating in the County Employee Retirement System (CERS). As a participating member, Lyon District is required to contribute a percentage of its employee wages to CERS. In the fiscal year beginning July 1, 2022, the CERS contribution rate will be 26.79 percent.<sup>28</sup> The CERS pension expense Lyon District reported in the test year conformed to the requirements of the Governmental Accounting Standards Board Statement No. 68 (GASB 68).

In its Application, Lyon District proposed to decrease its Employee Pensions and Benefits Expense by \$69,140 to reflect the amount Lyon District reported as expenses

<sup>27</sup> Case No. 2019-00268, *Application of Knott County Water and Sewer District for an Alternative Rate Adjustment* (Ky. PSC Mar. 24, 2020). Case No. 2020-00167, *Electronic Application of Ohio County Water District for an Alternative Rate Adjustment* (Ky. PSC Mar. 5, 2021). Case No. 2020-00296, *Electronic Application of Allen County Water District for an Alternative Rate Adjustment* (Ky. PSC Feb. 3, 2021).

<sup>28</sup> Kentucky Retirement Systems, Contribution Rates. ([Contribution Rates - Kentucky Public Pensions Authority](#))

its proportional share of its net pension liability.<sup>29</sup> However, upon review of the general ledger, Commission Staff determined that \$69,140 was the total expense recorded for the test year.<sup>30</sup>

In Case No. 2016-00163,<sup>31</sup> Commission Staff discussed in great detail how reporting requirements for GASB 68 would affect a utility’s income statement and balance sheet. In that proceeding, Commission Staff found that the annual pension expense should be equal to the amount of a district’s contributions to CERS, which “historically have been fairly constant.” Consistent with Commission Staff’s previous practice, Commission Staff decreased Employee Pensions and Benefits Expense by \$27,883.

| <u>Employee Pensions</u>                                   |                           |
|--|---------------------------|
| Pro Forma Salaries and Wages- Employees                    | \$ 154,002                |
| Multiplied by: Employer Contribution Rate Fiscal Year 2022 | <u>26.79%</u>             |
| Pro Forma CERS- Employer Contribution                      | 41,257                    |
| Less: Test Year CERS Contribution                          | <u>(69,140)</u>           |
| Employee Pensions and Benefits Adjustment                  | <u><u>\$ (27,883)</u></u> |

(G) Taxes other than Income - FICA. During the test year Lyon District reported \$0 to its Taxes other than Income.<sup>32</sup> However, Lyon District reported payroll

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<sup>29</sup> Application, Exhibit C, Adjustment D.

<sup>30</sup> Lyon District’s Response to Commission Staff’s First Request (filed Jan 28, 2022), Item 1g.

<sup>31</sup> Case No. 2016-00163, *Alternative Rate Adjustment Filing of Marion County Water District* (Ky. PSC Aug. 11, 2016), Staff Report on Marion County Water District at 11–27.

<sup>32</sup> Application, Exhibit C.

taxes of \$12,378 on the 2020 trial balance which were included in Employee Pensions and Benefits expense on the annual report.<sup>33</sup> Typically, it is proper accounting practice to classify payroll taxes as Taxes Other than Income on the annual report that is submitted to the Commission. Therefore, Commission Staff reduced Employee Pensions and Benefits by \$12,378, and increased Pro Forma payroll taxes of \$11,781 to Taxes Other Than Income, which was calculated utilizing the Pro Forma Salaries and Wages expense outlined in Adjustment (D) above, which effectively reclassified the expense. The calculation of pro forma payroll taxes is shown in the table below.

| Taxes other than Income- FICA          |            |
|--|------------|
| Pro Forma Salaries and Wages-Employees | \$ 154,002 |
| Times: 7.65 Percent FICA Rate          | 7.65%      |
| Pro Forma FICA                         | \$ 11,781  |

(H) Purchased Water Adjustment. Lyon District proposed to increase purchased water expense by \$2,761.<sup>34</sup> The adjustment was the net result of two calculations. The first calculation was to increase purchased water attributable to increased costs. The second calculation, which is further described in Adjustment (I) below, was to reduce purchased water by disallowed water loss pursuant to Commission regulations.

Subsequent to the test year, three of Lyon District’s water suppliers implemented increases in the wholesale rate charges for an adjustment increasing Purchased Water

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<sup>33</sup> Lyon District’s Response to Commission Staff’s First Request, (filed Jan 28, 2022), Items 1a 202\_Trial Balance.pdf.

<sup>34</sup> Application, Exhibit C, Adjustment E.



adjustment is in accordance with Commission regulations that prohibit the recovery of expenses for water loss in excess of 15 percent.<sup>38</sup> Commission Staff agrees with Lyon District’s methodology. However, Commission Staff disagrees with Lyon District’s proposed adjustment amount. Lyon District’s proposed adjustment does not appear to consider the increased costs outlined in Adjustment (H). When Adjustment (H) is included in the calculation for expenses attributable to water loss, the results in a net decrease to Purchased Water Expense of \$18,926 as shown in the table below.

|                                    |                    |
|------------------------------------|--------------------|
|                                    | Purchased<br>Water |
| Pro Forma Purchased Water          | \$ 392,346         |
| Times: Water loss in excess of 15% | 4.82%              |
| Total Cost of Excess Water Loss    | <u>\$ 18,926</u>   |

(J) Contractual Services - Legal. In its application, Lyon District proposed an adjustment to decrease Contractual Services by \$55,622.<sup>39</sup> The adjustment is proposed, in part, to normalize the legal fees to a standard year. Lyon District reported test-year Contractual Services - Legal expense of \$68,370.<sup>40</sup> During, and subsequent to, the test year, Lyon District incurred legal expenses to oppose the proposed increase in

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<sup>38</sup> Commission regulation 807 KAR 5:066(6)(3), Unaccounted-for water loss. Except for purchased water rate adjustments for water districts and water associations, and rate adjustments pursuant to KRS 278.023(4), for rate making purposes a utility's unaccounted-for water loss shall not exceed fifteen (15) percent of total water produced and purchased, excluding water used by a utility in its own operations. Upon application by a utility in a rate case filing or by separate filing, or upon motion by the commission, an alternative level of reasonable unaccounted-for water loss may be established by the commission. A utility proposing an alternative level shall have the burden of demonstrating that the alternative level is more reasonable than the level prescribed in this section.

<sup>39</sup> *Id.*, Adjustment F.

<sup>40</sup> 2020 Annual Report at 50.

wholesale water charges proposed by the city of Princeton.<sup>41</sup> Lyon District provided Commission Staff with the amounts reported in 2017, 2018, 2019, and the 2021 for legal expenses.<sup>42</sup> Commission Staff removed the fees associated with the city of Princeton water case from the test-year expense<sup>43</sup> because the expenses incurred during the legal case are not expenses incurred during a typical year. Commission Staff agrees with the methodology of adjusting the test-year legal expense to a normalized year's expense; however, Commission Staff calculated a five-year average in order determine the normalized legal expenses of \$3,636 as shown below. Therefore, Commission Staff reduced Contractual Services-Legal by \$64,734.

| <u>Contractual Services- Legal Fees</u>  |                        |
|--|------------------------|
| 2017                                     | \$ 2,000               |
| 2018                                     | 2,720                  |
| 2019                                     | 2,820                  |
| 2020- Less Princeton Water Legal Fees    | 3,280                  |
| 2021- Less Princeton Water Legal Fees    | <u>7,362</u>           |
| 5 year Average- Legal Fees               | 3,636                  |
| Less: Test Year Professional Fees- Legal | <u>(68,370)</u>        |
| Professional Fees- Legal Adjustment      | <u><u>(64,734)</u></u> |

(K) Contractual Services – Accounting. As mentioned in Adjustment (J), in the application, Lyon District proposed an adjustment to decrease Contractual Services by \$55,622.<sup>44</sup> The remainder of the adjustment proposed is to account for an increase in

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<sup>41</sup> Case 2019-00444, *Electronic Proposed Adjustment of the Wholesale Water Service Rates of Princeton Water and Wastewater* (Ky. PSC Jun 14, 2020).

<sup>42</sup> Lyon District's Response to Commission Staff's Second Request (filed Mar 10, 2022), Item 6a.

<sup>43</sup> Lyon District's Response to Commission Staff's first Request, (filed Feb 10, 2022), Item 1a, 2020 General Ledger, at 52.

<sup>44</sup> *Id.*, Adjustment F.

the contract for accounting consultation fees. The contract for Thurman Campbell Group, PLC states that Lyon District will pay a monthly fee of \$6,635 for 2022; and the monthly fee shall increase 1.5 percent each year.<sup>45</sup> Lyon District reported a test year amount for accounting services of \$86,970.<sup>46</sup> Accordingly, Commission Staff decreased Contractual Services by \$2,800 as shown below.

| <u>Contractual Services- Accounting Consulting</u> |                          |
|--|--------------------------|
| Monthly Consultant Fee                             | \$ 6,635                 |
| Times 12 months                                    | <u>12</u>                |
| Total Pro Forma Professional Services- Accounting  | 79,620                   |
| Plus: Annual Audit Expense                         | 4,550                    |
| Less: Test Year Professional Services- Accounting  | <u>(86,970)</u>          |
| Contractual Services- Accounting Adjustment        | <u><u>\$ (2,800)</u></u> |

(L) Depreciation. In its application, Lyon District reported its test-year Depreciation Expense of \$317,163.<sup>47</sup> To evaluate the reasonableness of the depreciation practices of small water utilities, the Commission has historically relied upon the report published in 1979 by the National Association of Regulatory Utility Commissioners (NARUC) titled Depreciation Practices for Small Water Utilities (NARUC Study). When no evidence exists to support a specific life that is outside the NARUC ranges, the Commission has historically used the midpoint of the NARUC ranges to depreciate the utility plant. Upon examination, Commission Staff found several assets

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<sup>45</sup> Lyon District's Response to Staff's Second Request (filed Jan 28, 2022), Item 6b.

<sup>46</sup> Lyon District's Response to Staff's First Request (filed Feb. 10, 2022), Item 1a, 2020 General Ledger at 53.

<sup>47</sup> *Id*, Exhibit C.

not depreciated at the NARUC ranges midpoints. In this proceeding, Commission Staff found no evidence to support depreciable lives that vary significantly from the midpoint of the NARUC ranges. After further review of Lyon District’s plant ledger, Commission Staff decreased Lyon District’s Depreciation Expense by \$103,489 to \$213,674 as shown below

| <u>Asset Group</u>               | <u>Current Depreciation</u> | <u>Depreciation Adjustment</u> | <u>Pro Forma Depreciation</u> |
|----------------------------------|-----------------------------|--------------------------------|-------------------------------|
| Group: 101.01 Land               | -                           | -                              | \$ -                          |
| Group: 101.02 Equipment          | \$ 31,555                   | \$ (5,787)                     | \$ 25,767                     |
| Group: 101.03 Distribution Ln #1 | 48,587                      | (13,560)                       | 35,027                        |
| Group: 101.04 Distribution Ln #2 | 212,393                     | (76,466)                       | 135,927                       |
| Group: 101.05 Lake Barkley Line  | 401                         | (80)                           | 321                           |
| Group: 101.06 Water Tanks        | 14,464                      | (4,950)                        | 9,514                         |
| Group: 101.08 Building           | 1,963                       | (153)                          | 1,810                         |
| Group: 101.09 Vehicles           | 4,400                       | -                              | 4,400                         |
| Group: 101.10 Improvements       | 3,400                       | (2,493)                        | 907                           |
| Total:                           | <u>317,163</u>              | <u>\$ (103,489)</u>            | <u>\$ 213,674</u>             |

OVERALL REVENUE REQUIREMENT AND REQUIRED REVENUE INCREASE

The Commission has historically applied a DSC method to calculate the Overall Revenue Requirement of water districts and water associations. This method allows for recovery of (1) cash-related pro forma operating expenses; (2) recovery of depreciation expense, a non-cash item, to provide working capital;<sup>48</sup> (3) the average annual principal

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<sup>48</sup> The Kentucky Supreme Court has held that the Commission must permit a water district to recover its depreciation expense through its rates for service to provide internal funds for renewing and replacing assets. See *Public Serv. Comm’n of Kentucky v. Dewitt Water Dist.*, 720 S.W.2d 725, 728 (Ky. 1986). Although a water district’s lenders require that a small portion of the depreciation funds be deposited annually into a debt reserve/depreciation fund until the account’s balance accumulates to a required threshold, neither the Commission nor the Court requires that revenues collected for depreciation be accounted for separately from the water district’s general funds or that depreciation funds be used only for asset renewal and replacement. The Commission has recognized that the working capital provided through recovery of depreciation expense may be used for purposes other than renewal and replacement

and interest payments on all long-term debts; and (4) working capital that is in addition to depreciation expense.

|   | Lyon County<br>Water District | Commission<br>Staff |     |
|---|-------------------------------|---------------------|-----|
| Pro Forma Operating Expenses                      | \$ 1,205,792                  | \$ 1,098,553        |     |
| Plus: Avg. Annual Principal and Interest Payments | 290,723                       | 290,723             | (1) |
| Debt Coverage Requirement                         | 58,145                        | 58,145              | (2) |
| Overall Revenue Requirement                       | 1,554,660                     | 1,447,421           |     |
| Less: Other Water Revenues                        | -                             | (1,489)             |     |
| Interest and Dividend Income                      | -                             | (606)               | (3) |
| Revenue Required From Water Sales                 | 1,554,660                     | 1,445,326           |     |
| Revenue from Sales at Present Rates               | (1,356,345)                   | \$ (1,356,345)      |     |
| Required Revenue Increase                         | 198,315                       | 88,981              |     |
| Percentage Increase                               | 14.62%                        | 6.56%               |     |

1. Average Annual Principal and Interest Payments. At the time of the Commission Staff's review, Lyon District had one outstanding loan from the Kentucky Infrastructure Authority (KIA),<sup>49</sup> one outstanding loan from Kentucky Rural Water Finance Corporation (KRWFC),<sup>50</sup> and one outstanding waterworks revenue bond, Series 2016.<sup>51</sup> In its application, Lyon District requested recovery of the average annual principal and interest on its indebtedness based on a five-year average of the annual

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of assets. See Case No. 2012-00309, *Application of Southern Water and Sewer District for an Adjustment in Rates Pursuant to the Alternative Rate Filing Procedure for Small Utilities* (Ky. PSC Dec. 21, 2012).

<sup>49</sup> Case 2015-00376, *Application of Lyon County Water District for a Certificate of Public Convenience and Necessity to Construct, Finance, and Increase Rates Pursuant to KRS 278.023* (Ky. PSC Jan. 7, 2016).

<sup>50</sup> Case 2012-00430, *Application of Lyon County Water District to Issue Securities in The Approximate Principal Amount of \$1,385,000 for the Purpose of Refunding Certain Outstanding Revenue Bonds of the District Pursuant to the Provisions of KRS 278.300 and 807 KAR 5:001* (Ky. PSC Oct. 5, 2012).

<sup>51</sup> Case 2015-00376, *Application of Lyon County Water District for a Certificate of Public Convenience and Necessity to Construct, Finance, and Increase Rates Pursuant to KRS 278.023* (Ky. PSC Jan. 7, 2016).

principal, and interest and fee payments for the years 2022 through 2026.<sup>52</sup> Commission Staff agrees with the methodology Lyon District proposes. As shown below, Commission Staff calculated an Average Principal and Interest Payment of \$290,723.

| Annual Principal and Interest Payment |           |                 |              |                 |             |                 |                       |
|---------------------------------------|-----------|-----------------|--------------|-----------------|-------------|-----------------|-----------------------|
| Year                                  | #F12-02   |                 | Series 2013C |                 | Series 2016 |                 | Total                 |
|                                       | Principal | Interest & Fees | Principal    | Interest & Fees | Principal   | Interest & Fees |                       |
| 2022                                  | \$88,163  | \$ 37,866       | \$50,000     | \$ 36,003       | \$48,500    | \$ 32,151       | \$ 292,683            |
| 2023                                  | 89,935    | 35,873          | 50,000       | 33,728          | 50,000      | 31,229          | 290,765               |
| 2024                                  | 91,743    | 33,839          | 50,000       | 31,328          | 51,500      | 30,276          | 288,686               |
| 2025                                  | 93,587    | 31,765          | 55,000       | 28,945          | 53,000      | 29,297          | 291,594               |
| 2026                                  | 95,468    | 29,648          | 55,000       | 26,924          | 54,500      | 28,347          | 289,887               |
| Total                                 |           |                 |              |                 |             |                 | 1,453,615             |
| Divide by: 5 years                    |           |                 |              |                 |             |                 | <u>5</u>              |
| Average Annual Interest Payment       |           |                 |              |                 |             |                 | <u><u>290,723</u></u> |

2. Additional Working Capital. The DSC method, as historically applied by the Commission, includes an allowance for additional working capital that is equal to the minimum net revenues required by a district's lenders that are above its average annual debt payments. In its application, Lyon District requested recovery of an allowance for working capital that is equal to 120 percent of its average annual debt payments for its loan payable to KIA at the time of its application.

<sup>52</sup> Application, Exhibit D.1.

|   |    |                  |
|---|----|------------------|
| Average Annual Principal and Interest       | \$ | 290,723          |
| Times: DSC Coverage Ratio                   |    | <u>120%</u>      |
| Total Net Revenues Required                 |    | 348,868          |
| Less: Average Annual Principal and Interest |    | <u>(290,723)</u> |
| Additional Working Capital                  | \$ | <u>58,145</u>    |

3. Interest and Dividend Income. In its application, Lyon District reported \$0 Interest Income in the revenue requirement calculation.<sup>53</sup> The Trial Balance includes Account #419.00 Interest Earned of \$606.<sup>54</sup> The DSC method to calculate the Overall Revenue Requirement does not allow for the recovery of Interest and Dividend Income; Therefore, Commission Staff reduced the Overall Revenue Requirement by \$606.

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<sup>53</sup> Application, Exhibit D.

<sup>54</sup> Lyon District's Response to Commission Staff's First Request (filed Feb 10, 2022), Item 1a, Trial Balance.

Signatures

/s/ William Foley

Prepared by: William Foley  
Revenue Requirements Branch  
Division of Financial Analysis

/s/ Ariel Miller

Prepared by: Ariel Miller  
Revenue Requirements Branch  
Division of Financial Analysis

/s/ Eddie Beavers

Prepared by: Eddie Beavers  
Rate Design Branch  
Division of Financial Analysis

/s/ Samuel Leveridge

Prepared by: Samuel Leveridge  
Rate Design Branch  
Division of Financial Analysis

APPENDIX

APPENDIX TO A COMMISSION STAFF’S REPORT OF THE KENTUCKY PUBLIC SERVICE COMMISSION IN CASE NO. 2021-00391 DATED APR 06 2022

The following rates and charges are prescribed for the customers in the area served by Lyon County Water District. All other rates and charges not specifically mentioned herein shall remain the same as those in effect under the authority of the Commission prior to the effective date of this Order.

Monthly Water Rates

5/8- x 3/4-Inch Meter

|       |                |         |              |
|-------|----------------|---------|--------------|
| First | 2,000 Gallons  | \$27.45 | Minimum Bill |
| Next  | 3,000 Gallons  | 0.01172 | Per Gallon   |
| Next  | 5,000 Gallons  | 0.00840 | Per Gallon   |
| Next  | 10,000 Gallons | 0.00706 | Per Gallon   |
| Over  | 20,000 Gallons | 0.00627 | Per Gallon   |

1-Inch Meter

|       |                |          |              |
|-------|----------------|----------|--------------|
| First | 15,000 Gallons | \$129.95 | Minimum Bill |
| Next  | 5,000 Gallons  | 0.00706  | Per Gallon   |
| Over  | 20,000 Gallons | 0.00627  | Per Gallon   |

1 1/2-Inch Meter

|       |                |          |              |
|-------|----------------|----------|--------------|
| First | 25,000 Gallons | \$176.62 | Minimum Bill |
| Over  | 25,000 Gallons | 0.00627  | Per Gallon   |

2-Inch Meter

|       |                |          |              |
|-------|----------------|----------|--------------|
| First | 45,000 Gallons | \$317.92 | Minimum Bill |
| Over  | 45,000 Gallons | 0.00627  | Per Gallon   |

Nonrecurring Charge

|                               |         |
|-------------------------------|---------|
| Meter Read-Out                | \$7.00  |
| Field Collection              | \$7.00  |
| Meter Reconnect               | \$10.00 |
| Meter Re-Read                 | \$7.00  |
| Meter Test                    | \$37.00 |
| Returned Check                | \$31.00 |
| 5/8- x 3/4-Inch Meter Tap Fee | \$1,022 |
| 1-Inch Meter Tap Fee          | \$1,382 |

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